



3rd quarter 2008

# Tennessee Housing Market

Business and Economic Research Center • David A. Penn, Director • Jennings A. Jones College of Business • Middle Tennessee State University

This is the fifth in a series of quarterly reports on the housing market in Tennessee, supported by a Tennessee Housing Development Agency grant.

## Third Quarter Economic Overview

Tennessee's economy continued to weaken during the third quarter due to continuing declines in housing construction, a faster pace of job losses in manufacturing, rising foreclosures, and the spread of job losses to the services-providing sectors. Perhaps the single most important indicator is the rise of the unemployment rate to 6.9 percent from 6.1 percent in the second quarter (Table 1). The most recent monthly unemployment rate (September) is 7.2 percent, the highest experienced by the state since 1983 and among the top 10 of the 50 states. Most of the states experiencing high unemployment are those strongly tied to either the real estate bust or the auto industry.

Manufacturing is a primary source of the job losses, due mostly to reductions in force in auto parts manufacturing and fabricated metal products. With the nation's fifth largest concentration of motor vehicle assembly and auto parts manufacturing,<sup>1</sup> Tennessee's economy is beginning to show the effects

of the difficult sales environment experienced by both domestic and foreign auto makers.

Retail trade, trucking, and warehousing also lost jobs in the third quarter, showing the effects of the sudden decline in consumer spending that has shaken retailers across the country. With fewer goods sold, retailers are cutting spending on new inventory and curtailing demand for transportation and warehousing services needed to move and store the goods.

The slowdown has produced sudden, unexpected declines in state government general revenue, with tax revenue collections for the first quarter of the fiscal year substantially lower than estimated. Additional budget cuts are expected for the remaining months of the current fiscal year; in addition, the state may dip into its rainy day fund for the first time during this revenue shortfall.<sup>2</sup> Present rainy day fund balances are about \$750 million, with an additional balance of \$500 million in Tenn-Care, the state's health care plan for eligible needy families.

## Housing Construction

Single-family home construction resumed its downward trend in the third quarter, dropping 11.6 percent from the sec-

**Table 1. Selected Tennessee employment indicators (thousands, seasonally adjusted)**

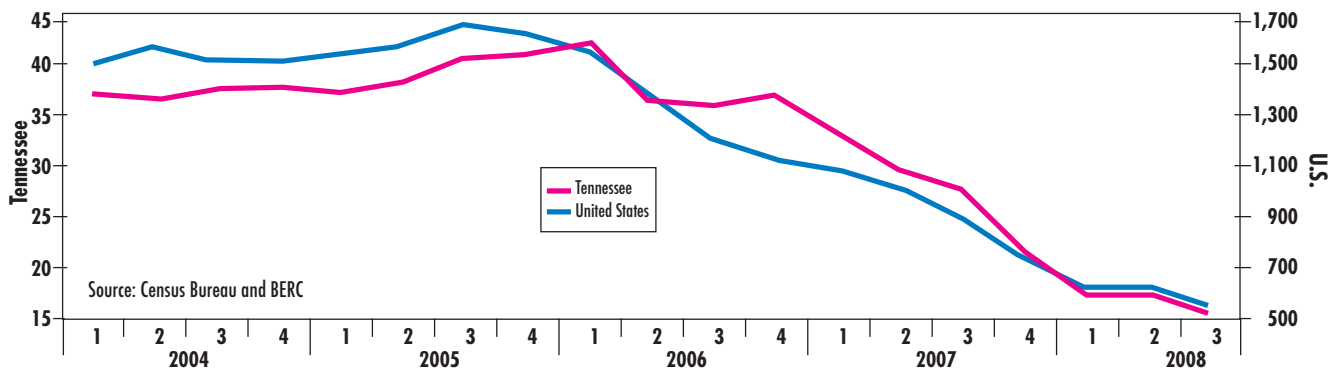
	2007.3	2007.4	2008.1	2008.2	2008.3
<b>Employment by industry (nonfarm)</b>					
Total nonfarm	2,804	2,803	2,797	2,785	2,785
Goods-producing sectors	516	516	512	508	506
Manufacturing	378	377	374	371	369
Services-providing sectors	2,287	2,287	2,284	2,276	2,279
Unemployed	144	152	160	186	209
Total employment	2,900	2,901	2,896	2,873	2,831
Labor force	3,044	3,054	3,057	3,058	3,041
Unemployment rate (percent)	4.7	5.0	5.2	6.1	6.9

Source: Bureau of Labor Statistics

**Table 2. Permits issued for privately owned new housing, seasonally adjusted annual rate (thousands)**

Quarter	Single-Family Permits			Total Permits		
	Tennessee	South	U.S.	Tennessee	South	U.S.
2006.3	36.0	674.0	1,269.0	43.3	868.7	1,713.3
2006.4	36.9	635.0	1,178.7	41.5	813.3	1,581.0
2007.1	33.1	588.3	1,130.3	39.7	781.7	1,581.0
2007.2	29.9	540.7	1,052.3	36.7	742.7	1,481.3
2007.3	27.7	482.0	931.7	33.7	654.0	1,335.3
2007.4	21.8	399.7	764.0	31.4	569.3	1,160.0
2008.1	18.0	351.7	647.3	23.5	515.0	988.3
2008.2	17.8	331.7	633.3	21.0	472.7	1,032.7
2008.3	15.7	288.7	558.3	21.5	446.0	866.3
Change from previous quarter	-11.6%	-13.0%	-11.8%	2.4%	-5.6%	-16.1%
Change from previous year	-43.2%	-40.1%	-40.1%	-36.3%	-31.8%	-35.1%

Source: Census Bureau and BERC

**Figure 1. Trend of single-family permits (thousands), Tennessee and U.S. (seasonally adjusted annual rate)**

ond quarter (Table 2) at about the same pace experienced by the South and the U.S. Over the year, permits for single-family construction are down 43.2 percent, again not appreciably different from the South and U.S.

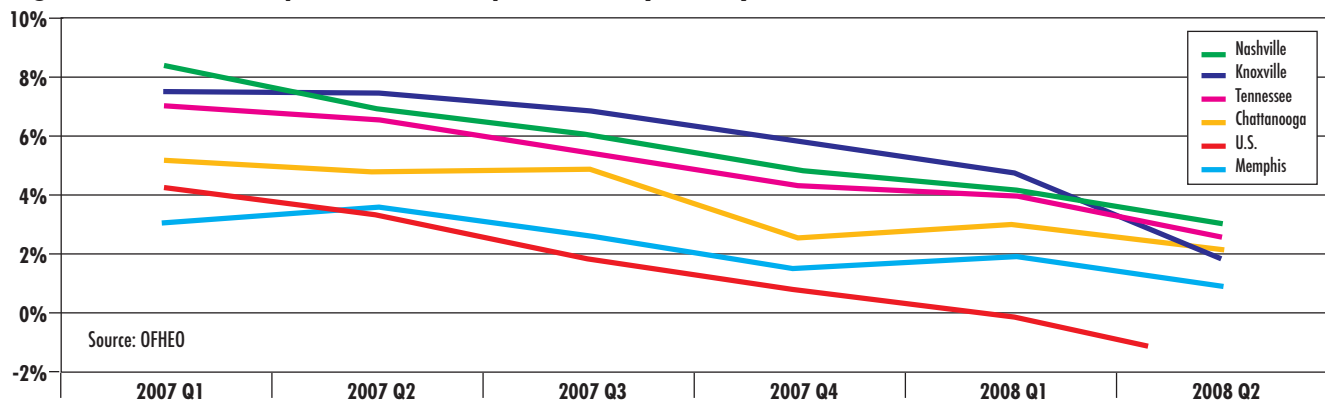
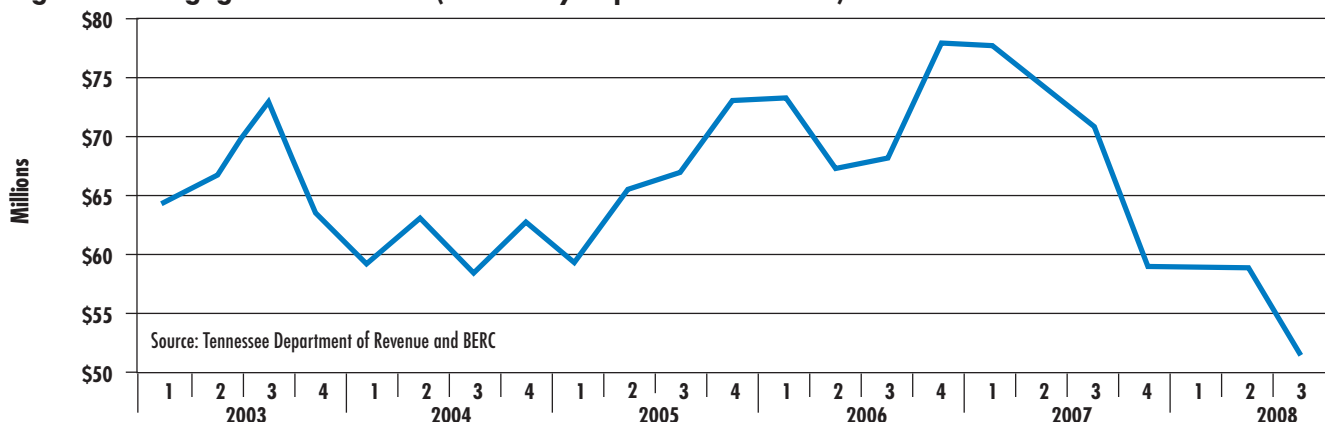
The picture is more positive when we examine total permits issued for housing construction, including both single- and multi-family permits. Total permits rose 500 units in the third quarter, a 2.4 percent gain. By contrast, the South and the U.S. show declines of 5.6 percent and 16 percent, respectively. The gain may be temporary for Tennessee.

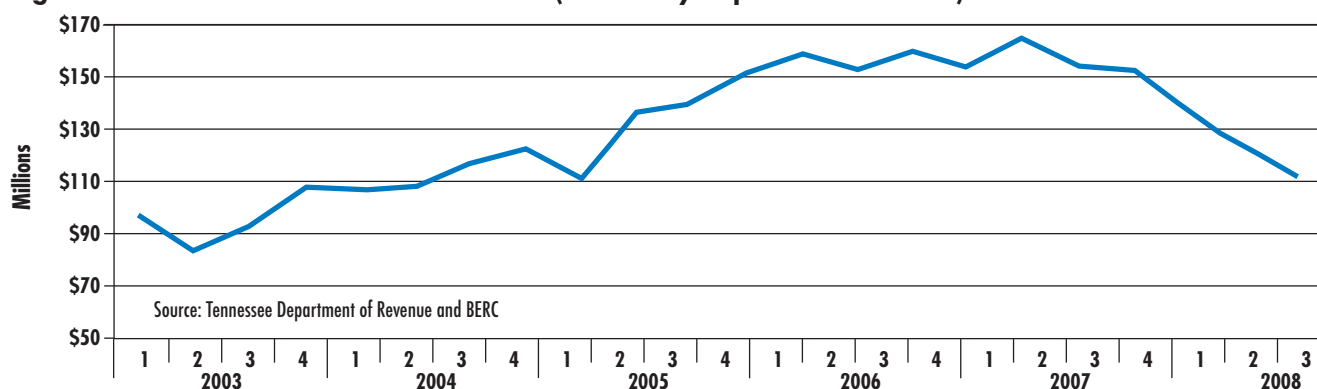
Forecasts by the National Association of Home Builders prepared last spring show a bottom in the fourth quarter of 2008

with slow growth in Tennessee for 2009. As of yet, however, no convincing signs are apparent for a turnaround in housing construction. Continuing population growth, particularly in middle Tennessee, helps to provide a floor for demand, but rising foreclosures, especially in the Memphis area, push more houses onto a market already in oversupply.

### Home Sales and Prices

The reduced supply of new homes on the market, as evidenced by falling housing construction, has helped to reduce the inventory of homes for sale in two of the major markets, Nashville and Memphis. In the Knoxville area, inventory is flat (non-in-

**Figure 2. Growth of repeat sales home price index, year to year****Figure 3. Mortgage tax collections (seasonally adjusted annual rate)**

**Figure 4. Real estate transfer tax collections (seasonally adjusted annual rate)**

creasing). A falling inventory helps to reduce the downward pressure on housing prices created by oversupply, thus helping to restore a balance between supply and demand over time.

Sales of homes show little improvement in the third quarter. Single-family homes improved slightly in Memphis but continued to drop in Knoxville and Nashville.

Prices have declined in several states that have large inventories of unsold homes, with California, Nevada, and Florida showing double-digit price declines over the year. In all, 20 states experienced price drops in the second quarter of 2008 compared with the previous year, according to figures from the Office of Federal Housing Enterprise Oversight (OFHEO).

According to comparable measures, Tennessee home prices are still rising but at a much slower pace. The fact that prices are not yet falling is a sign of strength in comparison with other states and the market nationally. Using figures from the OFHEO, prices of existing homes in Tennessee covered by Fannie Mae and Freddie Mac rose 2.7 percent over the year for the second quarter of 2008. By comparison, home prices nationally fell by 1.7 percent.

### Real Estate Transactions and Mortgages

Tax collections generated by real estate transfers and new or refinanced mortgages continued to plunge in the third quarter, with the transfer tax falling by 8.0 percent and the mortgage tax by 13.7 percent from the second quarter. Since peaking in the first quarter of 2007, the transfer tax has declined in all six subsequent quarters, while the mortgage tax has dropped in four of the six. Mildly positive news is that the third-quarter drop for

the real estate tax is smaller than the previous four quarters, suggesting real estate activity continues to fall but at a slower rate.

### Mortgage Delinquencies and Foreclosures

The number of new foreclosures in Tennessee took a turn for the worse in the second quarter, according to the most recent available data from the Mortgage Bankers Association of America. Following three quarters of modest increases, initial foreclosures experienced a substantial increase, rising to 0.78 percent of all mortgages serviced, up from 0.72 percent in the first quarter. The jump in new foreclosures caused the end-of-quarter inventory of foreclosures to climb to 1.58 percent of all mortgages, a recent high but still well below the 30-year high of 1.85 percent in 2003.

### Conclusion

Following a tepid second-quarter performance, the Tennessee economy weakened substantially in the third quarter. Rising unemployment, falling retail sales, accelerated job losses in manufacturing, and continued declines in housing construction signal the beginning of recession in Tennessee. On the positive side, home prices are holding up better than nationally, indicating local real estate markets will begin to show improvement before gains occur nationally. In addition, the diversity of the state's economy should help to cushion the impact of a national economic downturn. ■

1. As measured by auto assembly and parts manufacturing as percent of gross state product.

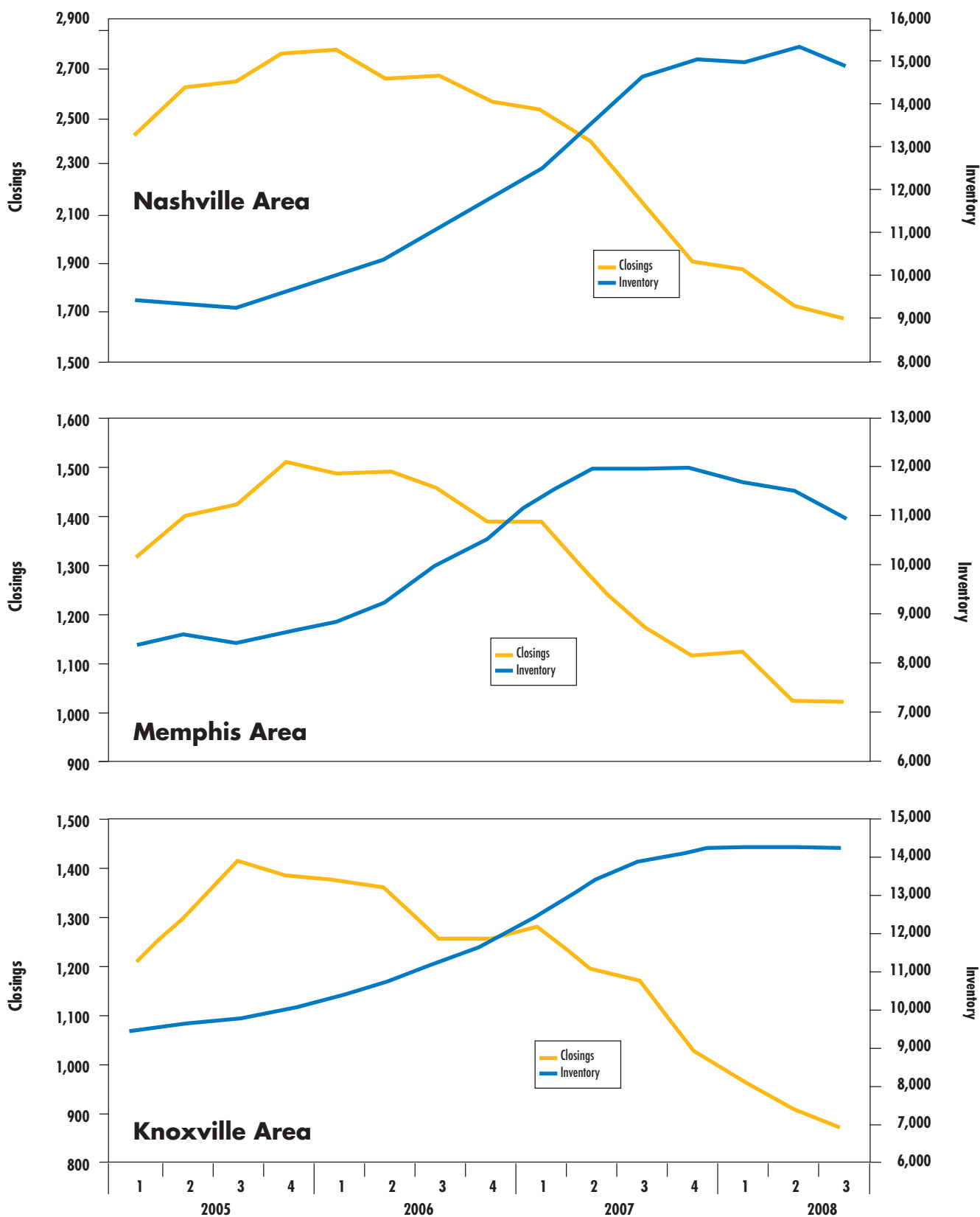
2. "Tennessee Likely to Tap Reserves" by Theo Emery, *Tennessean*, November 10, 2008.

**Table 3. Mortgages past due, new foreclosures started, and foreclosure inventory (% of mortgages serviced, seasonally adjusted)**

Quarter	Tennessee			U.S.		
	Mortgages past due	Foreclosures started during quarter	Foreclosure inventory at end of quarter	Mortgages past due	Foreclosures started during quarter	Foreclosure inventory at end of quarter
2007.1	6.54	0.60	1.24	4.88	0.58	1.26
2007.2	6.76	0.61	1.21	5.21	0.65	1.44
2007.3	7.43	0.69	1.27	5.55	0.77	1.71
2007.4	7.32	0.71	1.37	5.76	0.83	1.99
2008.1	7.82	0.72	1.49	6.36	1.00	2.44
2008.2	7.87	0.78	1.58	6.42	1.18	2.82

Source: Mortgage Bankers Association of America and BERC

Figure 5. Single-family sales and inventory (seasonally adjusted quarterly average of monthly figures)



Source: Greater Nashville Association of Realtors, Memphis Area Association of Realtors, Knoxville Area Association of Realtors, and BERC